

Testimony 1/11/07 Senate Bill 174

Mr. Chair, members of the committee. My name is George S Olsen. I represent the Montana Society of Certified Public Accountants.

The emphasis of Senate Bill 174 seems to be adding various new penalty provisions to the law. Professional tax preparers strive to accurately prepare income tax returns and in fact we are accused, mostly humorously, of working for the government by some of our clients. Our charge is to be aware of the law and apply the law appropriately. Our knowledge of the law and our role in the process actually enhances revenue to the State and the Federal government.

While we agree that there needs to be some penalty provisions in the law, we also feel that onerous penalty provisions can have the opposite result from that intended. Severe penalties can cause taxpayers to further delay completing and filing their returns and simply dig a deeper hole for themselves.

We have specific comments on individual provisions in Senate Bill 174. In general, we do not agree with many of the new or increased penalties. We are the ones that have to deliver the bad news to taxpayers.

In Section 3 (2)(a) the penalty is reduced from 1 ½ % to 1%. While we agree with a reduction, we do not feel that the reduction is enough when compared to the Federal rate of ½%. In addition, the "month or fractional month" phrase can subject the taxpayer to two months penalty for simply filing on May 1st -16 days after the due date. This has the effect of nearly quadrupling the penalty rate based on days outstanding. We further feel that there should be a safe harbor that the penalty is not assessed if the taxpayer has paid 90% of the tax by April 15th. This mirrors the Federal guideline and recognizes that the taxpayer may not have all information necessary to calculate the payment of 100% of the tax. In this case, the interest would still be assessed on the tax due when the return is filed.

In Section 3 (2)(b) we feel that the penalty limit of 15% is too high.

Section 3 (2)(c)(i) assesses a penalty for understatement of tax if the increase in tax is \$1500 which equates to a taxable income understatement of \$21,700. We feel that there should be a higher minimum amount for which there is no penalty. The \$1500 threshold is too low for understatements. There should also be a relief provision in the section.

We feel that the \$50 per incidence penalty in Section 3 (3) is not necessary or at least too severe. There is no meaningful definition of accurate reporting. Does a faulty zip code constitute an error subject to the penalty? Does a simple transposition cause the penalty to be assessed? The remedy period is not sufficient. Many tax returns are self prepared and to expect complete accuracy is not reasonable or fair to the taxpayer or selfishly, to the preparers. We all make mistakes. The income tax system is still based on voluntary compliance and this type of penalty does not reward the effort. The IRS has a program

that matches information from Form W-2's and Form 1099's for interest, dividends and other items with that reported on a taxpayer's return. The IRS program points out many simple errors and omissions but that information is not communicated to the taxpayer until more than a year after the fact. This is well beyond the deadline of six months. The penalty can cause significant penalties for small taxpayers and businesses with multiple information returns to issue.

We feel that the penalties in Section 3 (5)(a) and (b) are too severe. Two of our members likened that to a debtors prison. One year should be the maximum sentence. Do the violations need to be felonies?

Section 4 (11) deletes the language "or as that section may be labeled or amended." We are unclear as to why that phrase is deleted.

Section 6(1) adds a new tax on certain income of educational, religious or charitable trusts.

We are concerned that the new language in Section 8 may conflict with the Federal S Corporation rules regarding trusts. Qualified Subchapter S Trust shareholders need to conform to the Federal rules to maintain the S Corporation election.

We do agree with the amendments to Section 9 (2) regarding extensions of time to file tax returns.

We specifically do not agree with the restricted time for filing claims in new Section 10(2)(ii). The provision seems to change the statute of limitations for the taxpayer but not for the State. Both parties should be governed by the existing statute of limitations. If this provision is designed to allow the taxpayer additional time to file a claim beyond the existing statute of limitations in unusual cases, the language needs to be clarified as to form and intent.

Section 10 (4)(b) revises the interest to be paid on refunds of overpayments. Setting the deadline at the filing date for delinquent returns levies a double penalty on the taxpayer since the taxpayer has to pay interest from the original due date of the return as well as the late pay penalty but is entitled to interest only from the filing date.

Thank you for your time in allowing me to testify.